

offers separately priced extended warranty and service contracts to customers that extend and/or enhance the technical support, parts, and labor coverage offered as a part of the base warranty included with the product. The Company allocates fees from multiple element arrangements to the various elements based on the relative fair values of each element. Fair values are generally determined based on separate list prices. Product revenue is recognized when both title and risk of loss transfer to the customer, provided that no significant obligations remain. The Company provides for an estimate of product returns and doubtful accounts, based on historical experience. Revenue (net of estimated costs to be incurred) related to extended warranty and service contracts for which the Company is obligated to perform is recorded as deferred income and subsequently recognized on a gross basis over the term of the contract. Revenue from sales of separately priced third party extended warranty and service contracts for which the Company is not obligated to perform is recognized on a net basis at the time of sale. Professional services revenue is recorded when services are performed.

231. Defendants knew, or recklessly disregarded, that Dell's statements concerning its adherence to GAAP and its purported revenue recognition practices were false and misleading when made because, as described above, Dell failed to adhere to its stated revenue recognition policies and used "accounting adjustments . . . to compensate for earnings shortfalls that could not be closed through operational means." Moreover, Dell's restatement admits that the Company did not follow GAAP when reporting its financial results during the Class Period.

232. In commenting on Dell's Warranty accounting practices, the 2003 10-K stated:

Warranty — Dell records warranty liabilities for the estimated costs that may be incurred under its basic limited warranty as well as under separately priced extended warranty and service contracts for which Dell is obligated to perform. These liabilities are accrued at the time product revenue is recognized. The specific warranty terms and conditions vary depending upon the product sold and country in which Dell does business, but generally includes technical support, repair parts and labor and a period ranging from 90 days to three years. Factors that affect Dell's warranty liability include the number of installed units currently under warranty, historical and anticipated rates of warranty claims on those units and cost per claim to satisfy Dell's warranty obligation. The anticipated rate of warranty claims is the primary factor impacting Dell's estimated warranty obligation. The other factors are relatively insignificant because the average remaining aggregate warranty period of the covered installed base is approximately 20 months, repair parts are generally already in stock or available at pre-determined prices, and labor rates are generally arranged at pre-established amounts with service providers. Warranty claims are relatively predictable based on historical experience of failure rates. Each quarter, Dell reevaluates its

estimates to assess the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

233. Defendants knew, or recklessly disregarded, that these statements were false and misleading when made because, as described above, Dell accelerated the recognition of at least some deferred revenue from extended warranties and under-accrued costs associated with basic warranties in violation of GAAP.

234. The 2003 10-K also disclosed the following warranty-related information:

*Aggregate Product Warranty Liability* — Changes in the Company's aggregate product warranty liability are presented in the following table:

	Fiscal Year Ended January 31, 2003
	(in millions)
Aggregate liability at beginning of period	\$ 850
Cost accrued for standard warranties and separately priced extended warranty and service contracts issued during the period	1,327
Obligations honored during the period	(868)
Aggregate liability at end of period	\$ 1,309
Current portion	\$ 674
Noncurrent portion	635
Aggregate liability at end of period	\$ 1,309

235. Defendants knew, or recklessly disregarded, that this statement was false and misleading when made because, as described above, Dell accelerated the recognition of at least some deferred revenue from extended warranties and under-accrued costs associated with basic warranties in violation of GAAP.

236. In commenting on Dell's controls, the 2003 10-K stated:

Under the supervision and with the participation of Dell's management, including Dell's Chief Executive Officer and Chief Financial Officer, Dell has evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rule 13a-14(c) under the Securities Exchange Act of 1934) within the 90 days prior to the date of this Report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that these disclosure controls and procedures are effective in enabling Dell to record, process, summarize and report information required to be included in Dell's periodic SEC filings within the required time period. There have been no significant changes in Dell's internal controls or in other factors that could significantly affect internal controls subsequent to the date that Dell completed its

evaluation.

237. The Defendants knew, or recklessly disregarded, that the foregoing statement regarding Dell's controls was materially false and misleading when made. As admitted by Dell in its restatement, the Company failed to maintain effective controls which led to, *inter alia*, Dell employees using accounting "adjustments" in order "to compensate for operational shortfalls." In its restatement, Dell also admitted that its control deficiencies led to: a failure by the Company to consistently adhere to GAAP; a failure by the Company to employ persons with appropriate accounting knowledge given the complexity of Dell's reporting requirements; and a failure by the Company to maintain effective controls over period-ending reporting.

238. The 2003 10-K also included signed certifications from Michael Dell and Schneider which stated:

1. I have reviewed this annual report on Form 10-K of Dell Computer Corporation;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
  - b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this

annual report (the "Evaluation Date"); and

c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date.

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

239. The 2003 10-K also included signed certifications from Michael Dell and Schneider pursuant to Section 906 of the Sarbanes-Oxley Act which certified that: "(a) the Company's Annual Report on Form 10-K for the fiscal year ended January 31, 2003, as filed with the Securities and Exchange Commission (the 'Report'), fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 and (b) information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company."

240. Michael Dell and Schneider knew, or recklessly disregarded, that the statements contained in their signed certifications filed with the 2003 10-K were materially false and misleading when made because, as admitted by Dell in its restatement, the Company failed to maintain effective controls which led to, *inter alia*, Dell employees using accounting

“adjustments” in order “to compensate for operational shortfalls.” In its restatement, Dell also admitted that its control deficiencies led to: a failure by the Company to consistently adhere to GAAP; a failure by the Company to employ persons with appropriate accounting knowledge given the complexity of Dell’s reporting requirements; and a failure by the Company to maintain effective controls over period-ending reporting. Additionally, Michael Dell and Schneider’s Section 906 certifications were false because Dell has itself declared, “our previously issued financial statements for Fiscal 2003, 2004, 2005, and 2006 (including the interim periods within those years), and the first quarter of Fiscal 2007, should no longer be relied upon because of certain accounting errors and irregularities in those financial statements.” The foregoing statements are included in the periods Dell now admits are inaccurate and should no longer be relied upon.

241. The 2003 10-K also included a “clean audit” opinion from PwC which stated:

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Dell Computer Corporation and its subsidiaries at January 31, 2003 and February 1, 2002, and the results of their operations and their cash flows for each of the three fiscal years in the period ended January 31, 2003, in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the accompanying index, presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

242. PwC’s certification also assured investors that:

We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

243. PwC knew, or recklessly disregarded, that its statements in the 2003 10-K were materially false and misleading. As evidenced by Dell's restatement, the financial reports covered by PwC's foregoing "clean audit" opinion were materially false, required restating and, as cautioned by Dell, "should no longer be relied upon because of certain accounting errors and irregularities in those financial statements." Moreover, as explained *infra* at Section X, PwC's audit of Dell failed to comply with GAAS.

**E. First Quarter 2004 (For The Quarter Ended May 2, 2003)**

**1. First Quarter 2004 Earnings Release**

244. On May 15, 2003, Dell issued an earnings release announcing its financial results for the quarter ended May 2, 2003 (the "Q1 2004 Earnings Release"). The Q1 2004 Earnings Release, which was also filed with the SEC on Form 8-K, touted Dell's performance for the quarter as "its best-ever fiscal first-quarter operating results, recording exceptional growth and profitability in all product and regional markets. . . ." The Q1 2004 Earnings Release further informed investors that Dell's "second-quarter increases should also be strong." The Q1 2004 Earnings Release also contained the following false and misleading financial information relating to the Company's first quarter results:

	In Millions of Dollars (except per share data)
Net Revenue	\$9,532
Operating Income	\$811
Net Income	\$598
Gross Margin	\$1,748
Total Stockholders' Equity	\$5,076
Total Liabilities	\$10,636

245. In commenting on Dell's reported financial figures and its future prospects the Company stated:

First-quarter operating profit as a percent of revenue was 8.5 percent, Dell's highest in two and one-half years. Operating expenses were a record low 9.8



percent of revenue, down from 9.9 percent a year ago.

246. Defendants knew, or recklessly disregarded, that Dell's reported net revenue, operating income, net income and gross margin figures were misstated because, as admitted by Dell's restatement, the Company improperly recognized revenue throughout the Class Period and used "accounting adjustments . . . to compensate for earnings shortfalls that could not be closed through operational means." As a result of the Company's fraudulent revenue recognition practices, its reported stockholders' equity and total liabilities figures were also misstated. Moreover, as Dell has itself declared, "our previously issued financial statements for Fiscal 2003, 2004, 2005, and 2006 (including the interim periods within those years), and the first quarter of Fiscal 2007, should no longer be relied upon because of certain accounting errors and irregularities in those financial statements." The foregoing statements are included in the periods Dell now admits are inaccurate and should no longer be relied upon.

247. The Q1 2004 Earnings Release also included comments from Michael Dell that hailed the Company's reported results as an endorsement of the Company's products: "The words and actions of customers are clear. . . . They're recognizing the performance and reliability of standards-based enterprise computing, and choosing such servers and storage products at an accelerating rate. . . . Dell's unique ability is innovating, integrating and delivering technology with the best possible value, and our execution in those areas has never been better."

248. Michael Dell knew, or recklessly disregarded, that his statements about the Company were materially false and misleading because, rather than indicating an endorsement from Dell's customers, Dell's reported figures were the result of accounting manipulations intended to compensate for earnings shortfalls that could not be achieved through operational means.